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# Supreme Court of the United States

**OCTOBER TERM, 1935.**

**No. 533.**

DUPARQUET HUOT & MONEUSE CO., E. E. ALLEY CO., INC., and H. B. DAY CO., INC.,
*Petitioners,*

*vs.*

FRYSINGER EVANS, DU-WEL CLEANING CONTRACTING CO., GREENLEIGH PRINTING CO., INC., and GRAMERCY QUALITY LAUNDRY CO., INC.

## REPLY BRIEF FOR PETITIONERS.

HAROLD HARPER,
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## REPLY BRIEF FOR PETITIONERS.

### I.

Respondents contend (Brief, pp. 3, 14) "Since it is conceded that there is no such thing as a proceeding in equity receivership, the phrase is ambiguous and subject to construction." But why attribute to Congress an incongruity which the grammatical structure does not require, and without which there would be no ambiguity and no need for construction? The words are "if a prior proceeding in bankruptcy or equity receivership is not pending." The phrase has elsewhere been analyzed (Main Brief, p. 14), and there is no necessity of relating the word "proceeding" to "equity receivership". Certainly that could not have been done if the article "an" had preceded "equity receivership". Yet such language would have been equally acceptable to Congress. The House record of the Conference Report reads:

"On amendment No. 5: The Senate amendment, to which the House agreed, makes it unnecessary to show that

the corporation has committed an act of bankruptcy within four months in case a prior proceeding in bankruptcy or an equity receivership is pending at the time proceedings under the reorganization section are initiated." 78 Cong. Rec. 9898 [1934].

## II.

Nothing in the legislative record suggests that Congress intended to limit "equity receivership" to a suit of the conservation type. Even the mild statement of the court below (R., 20) that this *record* indicates "that the legislators were thoroughly familiar with this (conservation) type of receivership" appears mistaken. One reference (78 Cong. Rec. 7890) is to the debate over the provision permitting the filing of the petition in the jurisdiction of origin as well as in the jurisdiction of the principal place of business, which resulted in an amendment authorizing a transfer where the interests of the parties make it desirable. The other (78 Cong. Rec. 7905-7) is to the debate over the propriety of permitting Irving Trust Company to be sole receiver in bankruptcy in the Southern District of New York. Neither has anything to do with equity receiverships.

Respondents point out (Brief, pp. 8-9, footnote) that Representative McKeown in the course of hearings before the House Judiciary Committee explained that the bill *in its original form* had not conferred any remedy upon creditors, because creditors had the remedy of a federal receivership. From this respondents argue, though it seems a *non sequitur*, that when the remedy was subsequently given by amendment it was intended to be limited to cases in which there was bankruptcy or a receivership of the conservation type. This well illustrates the fallacy, pointed out in *United States* v. *Freight Association* (1897) 166 U. S. 290, 308, of arguing from the supposed views of individual legislators. If Representative McKeown entertained

any such view he certainly has changed it. In his book, McKeown & Langeluttig (1935) "Federal Debtor Relief Laws", he states that a foreclosure proceeding, "which involves the financial inability of a corporation to meet its debts", is such a proceeding as is contemplated by the act (pp. 112-115).*

## III.

It may be conceded that broader powers are usually conferred upon the receiver in a conservation suit than are usually conferred upon a receiver in a foreclosure suit (Brief, pp. 9-12). Such a distinction, however, is of no importance unless the words "equity receivership" are so uncertain as to be open to construction, and then only if a legislative purpose can be descried which would include the former and exclude the latter from the designation.

The Court will notice the large number of defaulted real estate bond issues.** The effect of excluding the foreclosure receivership as a basis of jurisdiction will be to limit the readjustment of these bond issues under 77B to cases where there is a board of directors ready, able and willing to help by filing a voluntary petition. The alternative is reorganization in the state courts or federal conservation suits. The former courts, lacking the bankruptcy power, operate under statutes of doubtful constitutionality or with the waste and expense attending foreclosure proceedings. The conservation type of suit has been denounced

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* The view of Representative McKeown in his book is somewhat different from that here advanced. He treats subdivision (i) as furnishing an *additional* ground of jurisdiction for an involuntary proceeding by creditors, and not as defining "equity receivership". He would permit a creditors' petition in the case of a foreclosure proceeding, "which involves the financial inability of a corporation to meet its debts", if a trustee or receiver is appointed for *all or any part* of the property of the corporation, and remarks that the provision of § 77B is in this respect broader than the provisions of the General Bankruptcy Act, 3(a)(5), 11 U. S. C. A. 21(a)(5).

** "The default in more than a majority of real estate bonds threatens investments estimated at eight billion dollars." 30 Columbia Law Review, 905 (June 1935).

in this court (Main Brief, p. 11), and is concededly unsatisfactory. As a commentator points out the problem is "whether the federal forum shall be denied to some groups and extended to others, solely because of the operation of fortuitous factors." 36 Columbia Law Review 153 (January 1936). True the affairs of a real estate corporation are local, but equally so are the affairs of an industrial corporation which happens to have a convenient creditor residing in another state. If there had been any legislative purpose to exclude corporations of a local character from the beneficent effects of 77B, voluntary petitions would have been excluded as well. If the decision of the court below is sustained, as pointed out in 30 Illinois Law Review 627 (January 1936), the many involuntary real estate reorganizations that are already pending under 77B will be thrown back into the state court or into conservation suits. This is too great a price to pay merely to preserve a supposed parallel between "equity receivership" and the receivership constituting an act of bankruptcy. Especially, when the supposed insufficiency of a foreclosure receivership to constitute an act of bankruptcy, if insolvency concurs, is based entirely upon the dictum in *Standard Accident Insurance Co. v. Sheftall & Co.* (5th C. C. A. 1931) 53 Fed. [2d] 40, 41.

## IV.

The idea that a creditors' petition will be looked at askance because the legislation is labeled "for the relief of debtors" (Section 77A, 11 U. S. C. § 206), is not in accordance with the views of the lower federal courts. These construed 77B as designed to relieve the debtor's creditors as well. As pointed out by Judge Mack in *In re Associated Gas & Electric Co.* (D. C., N. D. N. Y, 1935) 11 Fed. Supp. 359, 365 "this tag was attached to what was apparently the earliest draft bill" before any provision was made for creditors' petitions. He observes that, as the section was finally enacted, its scope was broadened by

the provision for involuntary petitions, and concludes "the interests of creditors as well as of the debtor are therefore to be considered in construing the language of the act." So Manton, C. J., in *In re 235 West 46th Street Co.* (2d C. C. A. 1935) 74 Fed. [2d] 700, 701, says:

> "It was the purpose of section 77B of the Bankruptcy Act to protect creditors and the debtor's equity in its property against possible injury traceable to frozen asset problems."

It has already been pointed out (Main Brief, pp. 22-23) that the corporation which allows a small portion of its property, the result of an unprofitable venture, to go the way of foreclosure, could not be subject to a creditors' petition unless the concomitant conditions were met of (1) insolvency, or inability to pay debts as they matured, and (2) a petition filed in good faith. It may be observed in addition that where, as in the case put (Respondents' Brief, pp. 15-16), the corporation has not assumed the mortgage indebtedness, failure of the corporation to perform the obligation secured by the mortgage will not even furnish evidence of its inability to meet debts as they mature.

Furthermore, the requirement that the petition must be filed in good faith as construed by the lower federal courts is no mere expression of a pious hope. There must be need for reorganization. *Manati Sugar Co.* v. *Mock,* (2d C. C. A. 1935) 75 Fed. [2d] 284, 285. There must be an actual intent to accomplish a reorganization. *In re South Coast Co.* (D. C. D. Del. 1934) 8 Fed. Supp. 43, 44. And there must be a probability that a reorganization can be effected. *Manati Sugar Co.* v. *Mock, supra; In re Grigsby-Grunow Co.* (7th C. C. A. 1935) 77 Fed. [2d] 200, 202; *In re Electric Public Service Co.* (D. C. D. Del. 1934) 9 Fed. Supp. 128.

If the courts follow these precedents, and if they observe the plain requirement of the statute that the debtor must

either be insolvent or unable to meet its debts as they mature, there is no fear that a comfortable corporation can be compelled to embark upon an unnecessary reorganization merely because it has suffered a portion of its property covered by an unassumed mortgage to be the subject of foreclosure receivership. See Gerdes "'Good Faith' in the Initiation of Proceedings Under Section 77B of the Bankruptcy Act" (1935) 23 Georgetown Law Journal 417-431.

The matter *dehors* the record (Brief, p. 17), which is inserted by way of "illustration" is quite immaterial in view of the fact that the rights of the parties must be determined as of the time when the petition was filed. *Bailey, Trustee* v. *Baker Ice Machine Co.* (1915) 239 U. S. 268, 275. It would be quite wrong, however, for the Court to draw the inference from the quite inadequate statement of the careening course of this corporation since the petition was dismissed below, that the debtor does not stand in need of reorganization, both in the interest of the petitioning and other creditors, who have not been paid, and in the interest of the bondholders of an earlier corporation on whose behalf the debtor was organized. Without accepting the invitation to wander from the record, suffice it to say that when this case comes to a hearing upon the facts it will not furnish a horrible example of the result of according to the language of a statute its literal and precise meaning, or of so construing a remedial statute as to promote the beneficial results at which it is aimed.

## V.

The President's Message, read January 11, 1933 (76 Cong. Rec. 1569) was in part as follows:

> "The process of forced liquidation *through foreclosure* and bankruptcy sales of the assets of individual

and corporate debtors who through no fault of their own are unable in the present emergency to provide for the payment of their debts in ordinary course as they mature, is utterly destructive of the interests of debtor and creditor alike, and if this process is allowed to take its usual course misery will be suffered by thousands without substantial gain to their creditors, who insist upon liquidation and *foreclosure* in the vain hope of collecting their claims. In the great majority of cases such liquidation under present conditions is so futile and destructive that voluntary readjustments through the extension or composition of individual debts and the reorganization of corporations must be desirable to a large majority of the creditors." (Italics ours.)

All four of the sections added by Chapter 28 to the Bankruptcy Act, 74 (compositions and extensions for individual debtors), 75 (agricultural compositions), 77 (railroad re-organizations), and 77B (corporate re-organizations) were responsive to that Message, although the last, originally incorporated in the bill, was for lack of time left over for the next Congress. If resort is necessary to the legislative record, it abundantly shows the intent of both houses to afford relief by these amendments against foreclosures. 76 Cong. Rec. 2931, 2941, 2913-14, 2915, 5107, 5127, 5358.

So do the sections themselves. Section 74 operated upon mortgagees and other secured creditors. They were made parties to the composition, the right of foreclosure was postponed and the bankruptcy court took jurisdiction of the mortgaged premises. Section 75 so far cut down the rights of mortgagees as to be held by this Court in violation of the Federal Constitution. *Louisville Bank* v. *Radford* (1935) 295 U. S. 555. The delay and expense incident to railroad foreclosures was one of the chief reasons for Section 77. *Continental Ill. Nat. B. & T. Co.* v. *C. R. I. & P. R. Co.* (1935), 294 U. S. 648, 685.

To interpret "equity receivership" as not including a case where the proceeding may end foreclosure and sale is to deny the very spirit and intent which animated Congress in passing all four sections amending the Bankruptcy Act.

It will be noted that the two sections relating to individuals do not provide for a petition by creditors. The threat of actual bankruptcy was no doubt thought a sufficient spur to induce the debtor to protect the rights of general creditors. The two corporate sections do provide for a petition by creditors, and this is obviously because the corporation may be unable or unwilling to help. But if the corporation is in receivership in a suit of the conservation type, it has already manifested its ability and willingness to help by admitting the allegations of the bill and joining in the prayer. *Re Metropolitan Railway Receivership* (1908), 208 U. S. 90. Of course it will file a petition under Section 77B, since there is no advantage to it in not doing so. Hence to limit the right of petitioning creditors of a solvent corporation to cases where the conservation type of proceeding is pending is to limit it to the type of case in which such right is least necessary.

Dated, New York, January 14, 1936.

Respectfully submitted,

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